BEFORE THE
PUBLIC SERVICE COMMISSION OF WISCONSIN

Application of Wisconsin Electric Power Company For Authorization to Implement New Electric Rates According to its 2017 Fuel Cost Plan

Docket No. 6630-FR-106

INITIAL BRIEF OF WISCONSIN ELECTRIC POWER COMPANY

In accordance with Wis. Stat. § 196.20(4) and Wis. Admin. Code § PSC 116.07, Wisconsin Electric Power Company seeks approval of its 2017 fuel cost plan. The plan estimates 2017 monitored fuel costs of $767,054,790, a decrease of $30.9 million—or 3.9%—from the fuel costs approved for 2016.[1]

Commission Staff reviewed Wisconsin Electric's work papers, books, records, other data and discovery responses supporting the estimated 2017 fuel costs and proposed several adjustments. (Ex.-PSC-Hillebrand-1). Wisconsin Electric and Staff addressed these and additional adjustments in rebuttal and surrebuttal testimony, and have reached agreement on all adjustments to Wisconsin Electric's as-filed fuel cost plan. (Rebuttal-WEPCO-Count-4p; Surrebuttal-PSC-Hillebrand-3pr:8-9).

Intervenors, however, dispute some of these agreed adjustments. The majority of these disagreements involve modeling assumptions adopted by Wisconsin Electric in the PROMOD runs underlying its fuel cost plan. Wisconsin Electric will first summarize the agreed-upon adjustments and then address the outstanding intervenor disagreement with those adjustments.

I. Staff's Proposed Adjustments to Wisconsin Electric's As-Filed Fuel Plan

[1] Based on numbers presented in Ex.-WEPCO-Count-4p, less final adjustments addressed at Surrebuttal-PSC-Ritsema-4:4 (modeled coal prices), Surrebuttal-PSC-Hillebrand-3cr:13 [redacted]), and Surrebuttal-PSC-Ritsema-3:6 (P4/Zion congestion), each of which is discussed below.

In their direct pre-filed testimony, Commission Staff proposed a total of eleven adjustments to Wisconsin Electric's as-filed fuel plan. (Ex.-PSC-Hillebrand-1). Of these, Wisconsin Electric agreed outright to all but Adjustments 3 and 5. (Rebuttal-WEPCO-Count-4p). Adjustment 3 concerned the fuel cost impact of the advanced gas path project at Port Washington Generating Station ("PWGS") Unit 2. (Ex.-PSC-Hillebrand-1). Wisconsin Electric and Staff agreed that the fuel plan should account for this project. However, due to recent developments in the project timeline, Wisconsin Electric proposed a further adjustment that would allow an *additional* $500,000 decrease on top of the decrease reflected in Staff's adjustment. This results in a total reduction of $1.6 million in monitored fuel costs as compared to the as-filed fuel plan. (Rebuttal-WEPCO-Count-5c).

The only other Staff adjustment initially in dispute was Adjustment 5, whereby Staff proposed increasing the assumed annual average blend of Powder River Basin ("PRB") coal at Elm Road Generating Station ("ERGS") to 78%. (Ex-PSC-Hillebrand-1; Direct-PSC-Hillebrand-2p-3p). In rebuttal, Wisconsin Electric explained that its as-filed fuel plan had assumed a PRB blend for the plant of approximately 65% for 2017, which alone would have reduced its monitored fuel costs by more than $5.7 million as compared to the costs authorized for 2016. (Rebuttal-WEPCO-Count-6p). Wisconsin Electric also explained the significant operational factors that would hinder pushing the ERGS PRB blend to 78% in 2017. (*Id.* at 7p-9p).

However, in acknowledgement of the issues identified by Staff, Wisconsin Electric proposed to increase its assumed fuel blend from 65% to 73% PRB, resulting in a decrease of $1.1 million *more* than the decrease resulting from the Staff adjustment—and a total reduction of

$8 million as compared to Wisconsin Electric's 2016 fuel case. (*Id.* at 9p).[2] Wisconsin Electric believes it can achieve a 73% PRB blend within the operational limitations referenced in Wisconsin Electric's rebuttal testimony. (*Id.*)

Commission Staff agreed with Wisconsin Electric's proposed modifications to Adjustments 3 and 5, both of which improved what were already significant cost reductions for ratepayers. (Surrebuttal-PSC-Hillebrand-2cr-3cr).

In addition, WIEG—which had originally proposed an ERGS PRB blend as high as 100% for 2017 (Direct-WIEG-Hennings-9)—came to agree with the 73% compromise reached by Wisconsin Electric and Staff. At the technical hearing, WIEG witness Ms. Hennings testified that of all the competing proposals for PRB blending at ERGS, the 73% PRB proposal represented the "least cost" alternative for Wisconsin Electric's customers. Transcript of Technical Hearing held Oct. 13, 2016 ("Hrg. Tr.") at 63-64. WIEG's agreement on this point solidified the consensus around a 73% average annual PRB blend at ERGS for 2017.

Finally, in surrebuttal testimony, Staff proposed one additional adjustment: [redacted] (Surrebuttal-PSC-Hillebrand-3cr). Wisconsin Electric does not oppose this additional adjustment.

As a result of Staff's proposed adjustments, as modified and agreed upon by Wisconsin Electric and Staff, Wisconsin Electric's customers will save an *additional* $13.9 million over and above the $17.0 million decrease from 2016 already assumed in Wisconsin Electric's as-filed fuel plan. (Direct-WEPCO-Count-4p).

II. Areas of Intervenor Disagreement

[2] The reason the fuel cost savings resulting from a 73% PRB blend at ERGS are *greater* than the savings resulting from a 78% blend is that the 73% blend results in fewer derates and fewer weeks of planned PRB inspection outages. (*Id.* at 9p-10p).

Over and above the adjustments proposed by Staff following their comprehensive audit, two intervenors—WIEG and Titus Energy—have identified what they view as additional deficiencies in Wisconsin Electric's fuel cost plan. Most of these perceived flaws relate to modeling assumptions adopted by Wisconsin Electric's fuel cost analysts in the PROMOD runs that form the basis of its fuel plan. It is not entirely clear how many of these issues remain unresolved as of this filing, but Wisconsin Electric will address the issues that appear most likely to remain in dispute, reserving the right to address any others in reply.

A. Escrow treatment for projected capacity sales revenues

Wisconsin Electric's fuel plan assumes a certain level of capacity sales revenues; these revenues, if they materialize, will offset Wisconsin Electric's fuel costs. Due to the recent volatility of pricing in the Midcontinent Independent System Operator ("MISO") capacity market and the uncertainty surrounding what prices will be in 2017, Staff's Adjustment 8 proposed using known 2016 capacity sales revenues as a proxy for 2017 revenues in Wisconsin Electric's fuel plan, subject to Commission-authorized escrow treatment for those revenues, which Staff witness Mr. Hillebrand noted would "equally protect both ratepayers and WEPCO." (Direct-PSC-Hillebrand-4p-5p). Wisconsin Electric agreed with this proposal. (Rebuttal-WEPCO-Count-4p). So did WIEG witness Ms. Maini, who further proposed dollar-for-dollar reconciliation once actual 2017 capacity sales revenues are known. (Direct-WIEG-Maini-5p).

The only party disputing the treatment of 2017 capacity sales revenues is Titus Energy, which opposed both escrow treatment *and* dollar-for-dollar reconciliation for capacity sales revenues, arguing that these revenues should be treated no differently than any others under the fuel rules in PSC 116 (i.e., subject to the 2% tolerance band). (Direct-Titus Energy-Vock-9-10; Rebuttal-Titus Energy-Vock-2-4). In response, Wisconsin Electric explained how escrow treatment benefits customers in this area of uncertainty, and that while treatment under the fuel rules may be reasonable for costs directly under Wisconsin Electric's control, escrow treatment is more appropriate here, where capacity sales revenues may vary widely from projections due to factors almost entirely *outside* Wisconsin Electric's control. (Surrebuttal-WEPCO-Count-5-6). Staff witness Mr. Hillebrand likewise reiterated Staff's view that full escrow treatment was warranted here. (Surrebuttal-PSC-Hillebrand-1pr-2pr).

At the technical hearing, following discussions with Staff, Wisconsin Electric proposed an alternative to full escrow treatment: exclude any bilateral sales from escrow treatment, subjecting them to the 2% tolerance band instead, but preserve escrow treatment for revenues from capacity offered into the MISO auction. (Hrg. Tr. at 30-31). This proposal recognizes that Wisconsin Electric has some control over the extent to which it sells capacity on a bilateral contract basis as opposed to selling it into the MISO capacity market. Under this approach, the escrowed amount would be equal to (1) the amount of capacity sold into the MISO capacity market times the difference between the projected and actual auction prices, *minus* (2) the difference (if any) between offered and sold capacity times the projected auction price—with any positive amount returned to customers and any negative amount collected from customers. (*Id.*)

Staff neither opposed nor accepted this proposal at the technical hearing. WIEG opposed it, continuing to argue for full escrow treatment because in its view, the alternative proposed by Wisconsin Electric would permit it to "game the system." (Hrg. Tr. at 64-65). WIEG has provided no support for this speculation, but ultimately Wisconsin Electric believes that it would be reasonable for the Commission to adopt *either* the full escrow treatment proposed by Staff and WIEG *or* the more nuanced approach proposed at the technical hearing.

B. Fuel case treatment of "uneconomic dispatch"

In its pre-filed testimony, Titus Energy voiced several related concerns around the concept of "uneconomic dispatch" as it relates to fuel costs at some of Wisconsin Electric's plants. None of these concerns led Titus Energy to articulate specific adjustments to Wisconsin Electric's fuel plan, but Wisconsin Electric addresses them to the extent Titus Energy invited the Commission to take some action, however defined.

First, Titus Energy claims that ERGS is being operated "uneconomically" year-round due to the Commission's waiver of Order Point 34 in Wisconsin Electric's 2012 rate case, which Titus Energy urges the Commission to reverse. (Direct-Titus Energy-Vock-12). Wisconsin Electric explained that the waiver merely permits it to *model* ERGS as offered into MISO as "must run," as opposed to "economic," that "economic" in this sense does not describe whether the plant is generating net revenues, and that modeling ERGS as offered into MISO as "must run" *improves* its performance from a revenue standpoint—a dispatch strategy that when employed in actual operations generated [redacted] in net revenues at ERGS last year alone. (Rebuttal-WEPCO-Count-13c-15c). This approach has benefitted customers, and Titus Energy has not demonstrated that Wisconsin Electric's modeling *or* dispatch strategy is imprudent.

Second, Titus Energy argues that the Commission should require Wisconsin Electric to identify which of its dispatch goes to serve customer load and which goes to "external sales," then identify which of its fuel costs are associated with which type of dispatch and realign its dispatch strategy so that the lowest-cost plants are dispatched first to serve customer load. (Direct-Titus Energy-Vock-13; Surrebuttal-Titus Energy-Vock-3-10). Simply put, this is impossible: Wisconsin Electric offers *all* of its available power into the MISO market, and MISO—not Wisconsin Electric—determines how best to meet system demand on an economic basis. Then, Wisconsin Electric buys back from MISO whatever power it needs to serve load within its service territory, again on a least-cost LMP basis. Within this system, there is no way to determine which fuel costs are associated with which types of load, as Titus Energy appears to assume. (Rebuttal-WEPCO-Count-16p-17p; Sur-surrebuttal-WEPCO-Count-4r-6r).

C. WIEG's preferred PROMOD assumptions

WIEG witness Ms. Hennings has taken issue with several of Wisconsin Electric's modeling assumptions in PROMOD. WIEG has not provided support for any of these alternatives in the form of adjustments to the fuel plan. Nevertheless, Wisconsin Electric briefly addresses WIEG's concerns and explains why its modeling assumptions—none of which were challenged by Staff—are reasonable.

1. Projected coal prices

Wisconsin Electric and Staff agree that the coal prices assumed in PROMOD should be those contained in the December 2015 release of the ABB Simulation Ready Data for the North American Electric Market, with a decrease of 5% for PRB coal and 10% for Bituminous coal. (Surrebuttal-PSC-Ritsema-3-4; Sur-surrebuttal-WEPCO-Count-2r). WIEG originally appeared to advocate *no* adjustments to the ABB data (Surrebuttal-WIEG-Hennings-2), but has not responded to the most recent adjustments agreed to by Wisconsin Electric and Staff, and has not reiterated an earlier proposal that coal price assumptions be based on 12 months of historical data instead of the ABB forecast (Direct-WIEG-Hennings-4). Wisconsin Electric assumes this disagreement has been resolved, but reserves the right to reply if it proves otherwise.

2. PWGS heat rates

In its initial testimony, WIEG took issue with the modeled heat rate for both units at PWGS. (Direct-WIEG-Hennings-4-5). Wisconsin Electric explained that it had increased this rate by 1-2% to account for a gas metering error identified by operators at PWGS. (Rebuttal-

WEPCO-Count-19p-20p). WIEG has not reiterated this concern in more recent testimony, so Wisconsin Electric assumes it is resolved.

3. Use of $4/MWh bid adder for combined cycle units

Wisconsin Electric's modeling used a $4/MWh off-peak bid adder for combined cycle units, another assumption challenged by WIEG, which argued that Wisconsin Electric should not be modeling bid adders that do not reflect how a unit is actually offered into MISO. (Direct-WIEG-Hennings-5-6).

In response, Wisconsin Electric explained that while it generally shares Ms. Hennings' preference to avoid bid adders, here the use of a $4/MWh off-peak bid adder is necessary to align modeled dispatch of these combined cycle units with historical data on actual dispatch. (Rebuttal-WEPCO-Count-20p-21p, including graph). Omitting the bid adders causes PROMOD to "choose" the units much more than historical data suggest they will be dispatched. (*Id.*)

WIEG's only reply was that the data relied on by Wisconsin Electric did not account for the 1-2% modeled heat rate adjustment at PWGS. (Surrebuttal-WIEG-Hennings-2). Wisconsin Electric agreed, but explained that including the heat rate adjustment would actually *support* using the bid adder: a slight increase to the units' heat rate would have slightly decreased their capacity factor, more closely aligning actual dispatch with the dispatch modeled *with* the bid adder . (Sur-surrebuttal-WEPCO-Count-2r). The record demonstrates that using a bid adder for the PWGS units is reasonable to align the model with real world experience.

4. P4/Zion congestion

The parties agree that transmission constraints at the Pleasant Prairie ("P4")/Zion node cause congestion costs, but disagree on how to capture or quantify those costs in the fuel plan. In Wisconsin Electric's last fuel case, Staff witness Mr. Ritsema developed a calculation that involved reconciling actual congestion costs with modeled congestion costs—a method that is generally acceptable to Wisconsin Electric. (Rebuttal-WEPCO-Count-21-22).

In this proceeding, WIEG witness Ms. Hennings has proposed addressing the problem through use of P4 dispatch adders instead. (Direct-WIEG-Hennings-7). While the theory behind Ms. Hennings' proposed approach is not entirely clear, it would seem to be that if congestion is the problem, her solution is to make P4 more costly to dispatch and therefore less likely to run in the model. (*Id.*; *see also* Rebuttal-WIEG-Hennings-5.)

Wisconsin Electric disagrees with this approach. Staff's Adjustment 6, as further modified by Mr. Ritsema in surrebuttal testimony, accounts for the congestion costs at issue using the method previously developed by Mr. Ritsema and does so without tampering with otherwise optimal dispatch through bid adders (whose use Ms. Hennings *opposes* for PWGS). (Direct-PSC-Hillebrand-3-4; Rebuttal-WEPCO-Count-21-22; Surrebuttal-PSC-Ritsema-2-3). The problems with Ms. Hennings' alternative approach are intensified by her more recent suggestion that the same bid adders *actually* be required as part of Wisconsin Electric's P4 offer strategy. (Rebuttal-WIEG-Hennings-5; Surrebuttal-WEPCO-Count-4-5). In short, Ms. Hennings failed to show why her indirect approach was superior to Mr. Ritsema's direct approach to accounting for the P4/Zion congestion costs.

5. $0.10/dekatherm gas hedging "premium"

Finally, WIEG challenges what it calls a $0.10/dekatherm "premium" on gas options used in Wisconsin Electric's modeling, arguing that Wisconsin Electric should not model this "premium" if it will not "charge" it in the hedging market. (Direct-WIEG-Hennings-10). But as Wisconsin Electric explained at some length, it is a price taker (not a price maker) in the options market, and this so-called "premium" is in fact a modeled ceiling on the risk that the actual price of gas options will exceed Wisconsin Electric's modeled assumption. (Rebuttal-WEPCO-Count-25-27). Understood as such, the $0.10 risk band is reasonable in light of historic price volatility in this market. (*Id.*) Notably, WIEG did not return to this issue in later rounds of testimony.

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For the foregoing reasons, Wisconsin Electric respectfully requests that the Commission approve its 2017 fuel plan, subject to the adjustments noted in the record and agreed upon by Wisconsin Electric and Staff.

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